

Attachment A

Long-Distance Pricing 1996—Yikes!

Michael T. Hills

Annual price hikes of 5 to 7 percent continue. In a world without tariffs, can you ever be sure you got a good deal?

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With the FCC proposing to end the tariffing of all long distance services, this could be the last year I write this article in its current form. Think about it: With none of the long distance carriers dominant, none will have to file tariffs.

On what data shall I base my comparisons and, more important, how will your organization determine if it is being charged appropriately? Sure, if you are big enough, you will always be able to

shop and compare and get the best deals, but I suspect smaller business and certainly residential customers will wind up paying more for fewer choices.

Rates Continue to Climb

While the alleged benefits of telecom deregulation—competition and lower prices—are assumed to accrue to all, the FCC will have its hands full for some time specifying the conditions under which full competition can unfold (see Vic Toth's column in *BCR*, March and April 1996, pp. 22-24 and 20-22, respectively, and in this issue, pp. 24-25). Meanwhile, this year's long distance pricing review shows another round of the relentless increases we have come to expect since the major interexchange carriers began raising their month-to-month rates for all types of long distance service in 1990.

The one exception, as shown in Table 1, is Sprint, which hasn't raised prices on VPN Premiere, its virtual network service. The per-minute rates in the table are exclusive of any special discounts, and show Sprint's VPN Premiere saving more than 10 percent over AT&T's OneNet and MCI's comparably priced WorldNet.

AT&T is still leading the industry—its 5 to 6 percent price increases are quickly followed by the other carriers. For example, Figure 1 (p. 36) tracks the average cost per minute for current integrated plan offerings—AT&T's Uniplan, MCI's Vision and Sprint's Clarity—compared with the carriers' older, dedicated outbound services: AT&T Megacom, MCI Prism I and Sprint Ultra-WATS service (no longer available to new customers). Between January 1990 and March 1996, these prices have increased by 24 to 35 percent.

Our calculations assume 1,000 hours per month of typically dispersed outgoing long distance traf-

	AT&T	MCI	Sprint
Off-Net/Off-Net	\$0.2686	\$0.2659	\$0.2522
Off-Net/On-Net	\$0.2048	\$0.2028	\$0.1823
On-Net/Off-Net	\$0.2058	\$0.2028	\$0.1823
On-Net/On-Net	\$0.1439	\$0.1424	\$0.1323
Average Rates as of 3/1/96	\$0.2022	\$0.2002	\$0.1806
Average Rates as of 1/1/95	\$0.1901	\$0.1884	\$0.1628
Percentage Increase 1/1/95 to 3/1/96	6.3%	6.3%	—
Average Rates as of 1-1-93	\$0.1660	\$0.1636	\$0.1586
Percentage Increase 1/1/93 to 3/1/96	21.8%	22.4%	15.3%

**Break-even points
for virtual
network services
continue to move
down**

FIGURE 1 Historical Pricing Trends

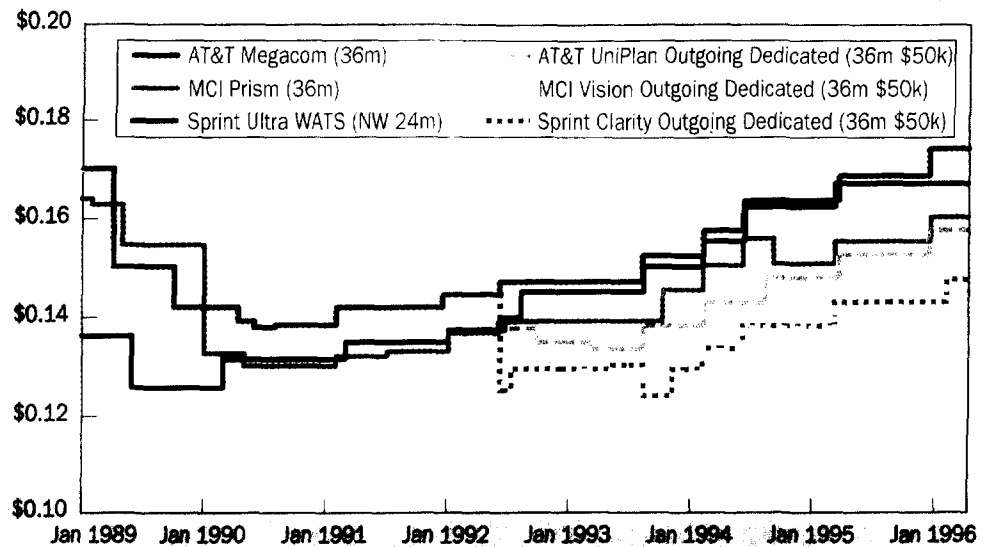
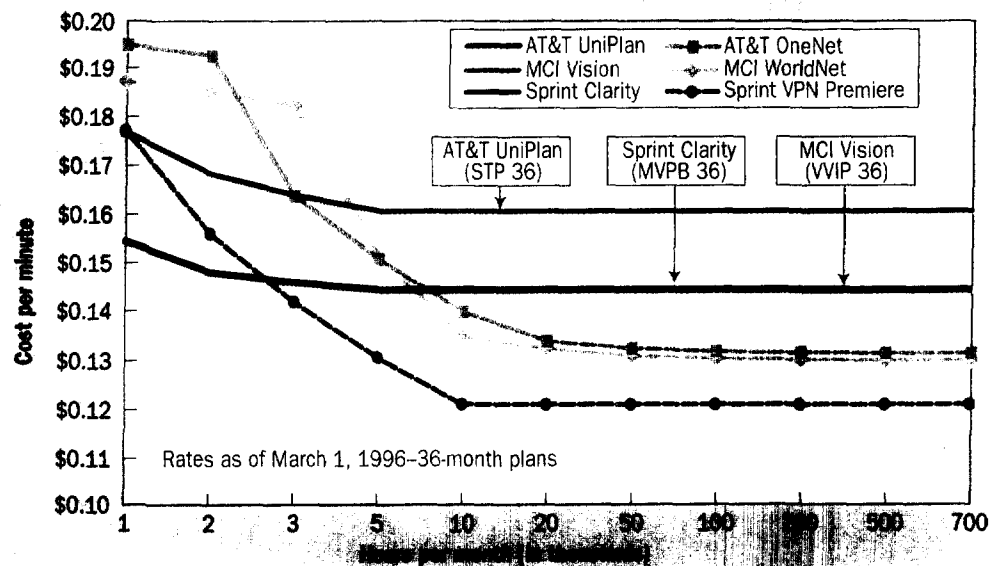


FIGURE 2 Cost Comparison: Virtual Networks and Integrated Pricing Plans



fic, via T1 access (cost of the T1 access is included). A 36-month contract commitment has been made, except for Sprint's old UltraWATS, which was offered only on a 24-month contract.

Figure 2 compares the cost per minute of the carriers' integrated plans with their virtual network plans. Per-minute prices are a penny or two higher across the board (except for Sprint Premiere), but the breakeven points—where virtual network plans cost less per minute than comparable integrated plans—continue to move down. Last year, we found AT&T's OneNet and MCI WorldNet competitive at 10,000 hours per month; this year, AT&T breaks even at 5,000 and MCI at about 7,500 hours per month. Sprint broke even at 5,000 hours per month last year and at 3,000 hours this year.

How We Got Here

It's probably a safe bet that these rates will continue their inexorable 5 to 7 percent per annum increases—we just may not be able to watch it happen on official tariffs any longer! Here's how this came to be:

1. Background: Ten years ago the FCC attempted to detariff nondominant long distance carriers (everyone but AT&T). MCI wanted to continue filing tariffs and appealed to the U.S. District court, which found that the FCC lacked the authority to prohibit carriers from filing tariffs, but could permissibly detariff. This issue went all the way to the Supreme Court, which, in 1994, found that the FCC could modify tariff filing requirements but not eliminate them. In 1995 the FCC required all carriers to file tariffs.

2. AT&T Reclassified as a Nondominant Carrier: After years of petitioning the FCC for nondominant status, AT&T was granted its wish in October 1995. Although the FCC found AT&T no longer possessed individual market power in the interstate, domestic, interexchange market as a whole, they deferred consideration of AT&T's power in the international market.

Prior to this ruling, AT&T was held to a higher standard: longer intervals between tariff filing and effective dates, stricter monitoring and so forth. Now AT&T will be treated no differently than its nondominant competitors. Specifically, these carriers must:

- Offer interstate services under rates, terms and conditions that are just, reasonable and not unduly discriminatory.
- File tariffs at least one day prior to their taking effect.
- Give notice prior to any discontinuance, reduction or impairment of service.
- Be subject to the Commission's complaint process.

To address concerns about possible adverse effects of its reclassification as nondominant, AT&T made certain voluntary commitments:

- For a period of three years, to offer optional calling plans to residential subscribers.
- For a period of three years, to limit rate increases to the CPI for analog private line and 800 directory assistance services.
- Prompt dispute resolution procedures for reseller customers.

For its part, the FCC stated in its order that it would consider the following issues relevant to the interstate, domestic, interexchange market as a whole in this proceeding:

- Whether there is tacit price coordination in the interexchange market.
- How changes in the interexchange market affect rate integration and geographic averaging.
- The concerns of resellers and large users regarding contract tariffs.
- The application of the filed rate doctrine to contract tariff arrangements.

3. Telecommunications Act of 1996 Changes All the Rules: On February 8, 1996, this Act—which seeks “to provide for a pro-competitive, deregulatory national policy framework” designed to make available to all Americans advanced telecommunications and information technologies and services “by opening all telecommunications markets to competition”—was signed into law (see *BCR*, March 1996, pp. 6, 14–16 and 22–24).

The Act completely changes the legal framework governing the interstate, interexchange market. Specifically, it promotes facilities-based competition in the interexchange market and opens the door for new entrants to compete with existing service providers. Its main points include:

A. The Bell Operating Companies (BOCs) can immediately provide interLATA service originating outside their own states.

B. BOCs can provide “incidental” interLATA services now, including:

- Audio and video programming (including interactive).
- Alarm monitoring services.
- Internet services over dedicated facilities to or for schools.
- Commercial mobile (cellular) services.
- Storage or retrieval of information from information storage located in another LATA.
- Transmission of signaling and network control information.

C. BOCs can provide interLATA services in their own areas soon. This is the most important provision, and the one most bitterly fought over. The gist is that after fulfilling certain specified preconditions, the BOCs may provide interLATA services originating inside their own states. The main condition is the BOCs must unbundle their local phone networks so competitors can buy and sell component parts and put together their own networks. Also the local phone companies must allow competitors' networks to interconnect with their own so that calls from one network can be terminated on any other. And all this must be done at a just and reasonable price.

The FCC has yet to issue rules implementing these provisions of the act, however, and lengthy battles are expected. The IXC's are clamoring for the BOCs to open their territories to competitive local service, one of the preconditions, while at the same time they do not want the BOCs competing in their interexchange markets.

The BOCs, meanwhile, will be as protective as is legally possible of their own territories, while trying to comply minimally, but sufficiently, to compete with the IXC's for interexchange long distance. So, don't expect your local BOC to be offering you long distance in the near future.

4. All Nondominant Interexchange Carrier Services to Be Detariffed: That's right, just four months after the FCC put AT&T on level ground with its other, nondominant competitors, the 1996 Act directs the FCC to “forbear from controlling” (i.e., detariff) all nondominant, interstate interexchange services, provided certain specified conditions are satisfied. The Act also specifies that the FCC could, however, require tariffs of dominant carriers if and when any emerge (perhaps certain BOCs in their territories; for example, if the Southwestern Bell purchase of Pacific Tel goes through).

Pros and Cons of Detariffing

The FCC has long held that requiring nondominant interexchange carriers to file domestic tariffs is unnecessary for consumer protection and, in fact, harms consumers by undermining the development of vigorous competition. It is proposing a mandatory detariffing policy for domestic services offered by nondominant interexchange carriers. Since the reclassification of AT&T, there are now no dominant interexchange carriers.

Don't expect your BOC to offer long distance in the near future

**Detariffing—
a retrograde step
for all but the
very largest
companies**

Note that this deregulation proposal applies to all interexchange interstate services, including private lines. The LECs are still regarded as dominant carriers for access, so the rates charged by the LECs to the IXC for origination and termination of calls will continue to be tariffed.

Some of the reasons given by the FCC as examples of how tariff-filing hampers competition include:

- It takes away carriers' ability to make rapid, efficient responses to changes in demand and cost.
- It impedes and removes incentives for competitive price discounting.
- It imposes costs on carriers that attempt to make new offerings.
- It presents an opportunity for collusive pricing by competing carriers, because carriers can ascertain their competitors' existing rates and keep track of any changes by reviewing filed tariffs.

In fact, the FCC believes tariff filing may actually encourage carriers to maintain rates at artificially high levels. Cynical observers might counter that the interests of consumers and small business are better served by government-controlled, tariffed and published services, and that these customers' interests have been sold out to further the deal-making prowess of the largest customers.

Large businesses will buy long distance services just as they buy fleets of cars—in both cases, they've got the power to get the best deals. In my opinion, detariffing is a retrograde step for all but these large companies.

For the rest of us, detariffing reduces the buying of long distance service to the terrible trauma of buying a new car. You know the sticker price but you are never sure whether you have received the best deal—you always leave the show room wondering if you got the best price.

When you buy gasoline for your car, you can drive around to compare prices; when you buy airline tickets, you can call the airlines or use a travel agent to identify your options—usually a tradeoff between price and convenience. Without tariffs, preparing the analyses presented in this type of article—and in your offices as you consider long-distance service options—will become much more difficult. At a minimum, it will be necessary to continually monitor the carriers' price lists—assuming they are made available.

On the positive side, when detariffing occurs, there will be several advantages to customers:

- Lower prices (they say).
- Fixed prices—the carriers will no longer be able to offer some percentage off tariff price and then routinely increase the tariff price once or twice a year. Perhaps postalized rates (like Sprint's 10 cents per minute) will become the norm.
- Removal of any restrictions on bundling customer premises equipment with carrier services. A customer will once again be able to lease a multiplexer or CSU/DSU equipment as part of its network service.
- A signed contract with a carrier will become enforceable—no underlying tariff's terms will supersede any written agreement.
- A carrier could be sued for consequential damages, which are currently excluded by tariff.

Perhaps it is those last two items that are keeping the carriers quite mum on the topic of detariffing at the moment. Could it be that they somewhat appreciated the "protection" of the government as well? Remember the fuss MCI put up the

last time the Commission tried to detariff nondominant carriers?

As to existing contract tariffs, the FCC is hoping to address and resolve their status in upcoming hearings. Note that the detariffing craze does not extend to the BOCs' long distance service entry. In fact, the Commission could decide that the BOC becomes a dominant interexchange carrier in its own area once it is permitted to provide long distance.

Conclusion

The question right now is, if you aren't on a vir-

tual network or integrated plan, should you be? And if so, how long a contract period should you commit to?

Based on the historical trends and most recent developments, we expect reference rates for integrated or virtual services to continue their annual increase of at least 5 percent per year. If you are not already on a plan filed within the last 12 months, you should consider transferring to one—now. There are savings to be had if you ask for them, and you should not let uncertainty deter you from minimizing your current costs.

If, however, you sign a five-year contract today that is covered by tariff, what will you be liable for when the tariff is canceled? Such questions will be hotly debated in the next few months in the FCC hearings. Keep your eye on the trade press and, of course, on BCR as this unfolds □

